(19)

No. 91-1135

Supreme Court, U.S.
FILED
JUN 5 1992
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

NEWARK MORNING LEDGER CO.,
as successor to The Herald Company,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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BRIEF OF PHILIP MORRIS COMPANIES INC. AS *AMICUS CURIAE* IN SUPPORT OF NEITHER PARTY

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INTEREST OF AMICUS CURIAE

A wholly-owned subsidiary of *amicus curiae* is appellee in a case currently pending before the United States Court of Appeals for the Second Circuit, *Philip Morris Incorporated* v. *Commissioner of Internal Revenue*, Second Circuit No. 92-4025, *on appeal from* 96 T.C. 606 (1991). The issue in *Philip Morris* is the correctness of findings of the United States Tax Court regarding valuation of the "goodwill" of The

Seven-Up Company at the time of its acquisition through an unsolicited public tender offer.

The parties in the instant case have stipulated to the value of the "goodwill" of the acquired newspapers. They thus have eliminated from consideration by this Court the issue presented in *Philip Morris*. Nevertheless, because of certain statements of the parties here, *amicus* is concerned that the issue of proper goodwill valuation may somehow be woven into the resolution of the instant case, thereby inadvertently affecting its pending case.

The written consents of the parties have been filed with the Clerk of this Court pursuant to Rule 37.

ARGUMENT

The instant case presents the question whether a particular intangible asset—referred to as the "paid subscribers" of an ongoing newspaper business—is a proper subject for depreciation under 26 U.S.C. § 167(a) or, rather, is a part of nondepreciable "goodwill."

The instant case does *not* present an issue as to the proper method of valuing the "goodwill" of the acquired newspapers. That is because the parties have stipulated that the method to be used to value that intangible asset is the so-called "residual method."[1] Pursuant to the stipulations of the parties, the value of the goodwill of the acquired newspapers will be

[1] In general, under the residual method, the price paid for a business is assumed to equal the value of the business's assets, the value of all assets other than goodwill is subtracted from the total price paid, and the residual amount is treated as the value of the goodwill.

the difference between a specified amount ($89,578,685) and the ascertained value of the paid subscribers if found to be depreciable. (Pet. App. 37a.) There will thus be no occasion for this Court to consider the propriety of the goodwill valuation.

Nevertheless, in its Brief on Petition for a Writ of Certiorari, the United States made two assertions that at least suggest the possibility that the proper method of valuing goodwill might somehow get placed before this Court in the instant case. Specifically, the United States stated that, in petitioner's allocation of purchase price among the acquired assets, goodwill was "required" to be assigned the remainder of the purchase price after all other assets (tangible and intangible) had been valued. (Brief for the United States on Petition for a Writ of Certiorari ("Cert. Br. U.S.") 2-3.) The United States also claimed that any "premium" paid for a business over and above what the tangible assets would be worth if bought individually is "associated with the going concern value or goodwill of the business." (Cert. Br. U.S. 15.) In addition, in its brief on the merits, petitioner uses the term "residual" in describing how goodwill should be defined and valued for purposes of Section 167. (*See, e.g.*, Brief of Petitioner Newark Morning Ledger Co. 3, 19, 37.)

As is clear from the relevant authorities, any suggestion that the residual method is the only appropriate way to value goodwill in all circumstances is incorrect. The law in effect when the acquisition here involved took place did not mandate use of the residual method to value goodwill. (*See, e.g., R.M. Smith, Inc.* v. *Commissioner*, 591 F.2d 248 (3rd Cir.), *cert. denied*, 444 U.S. 828 (1979); S. Rep. No. 313, 99th

Cong., 2d Sess. 252-253 (1986); *see also* Treas. Reg. Sec. 1.334-1(c)(4)(viii).) The parties here merely agreed to use that method.

Further, the Third Circuit in *R.M. Smith, supra,* has made it clear that a "premium" paid for the stock of a corporation, over and above the value of its tangible assets, would not inevitably represent the value of its goodwill and that the residual value method may be inapplicable "when one party to the transaction achieves a bargain." 591 F.2d at 252-253.

The issue in the pending *Philip Morris* case is the propriety of the Tax Court's conclusion that it was appropriate to value goodwill using the so-called "excess earnings" method based upon Rev. Rul. 68-609, 1968-2 C.B. 327, rather than the residual method.[2] *Philip Morris* involved an acquisition by unsolicited public tender offer where the total purchase price was found to include a "control premium" and the requisite equivalence called for in *R.M. Smith* between the price paid and the value of the assets was found not to be present.

Amicus thus wishes to make it clear that (a) the courts have rejected any suggestion that the residual method invariably was required for valuing the goodwill of a going business during the period here involved, and (b) in any event, the question of how to value goodwill is not now before this Court.

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[2] In general, under the "excess earnings" method, goodwill is valued by reference to the earnings deemed attributable to those intangible assets not separately valued.

CONCLUSION

For all of the foregoing reasons, *amicus* respectfully requests that this Court avoid possible confusion in this area by expressly indicating in its opinion that the proper method for valuing the goodwill of a going business is not at issue in the instant case.

Respectfully submitted,

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June 5, 1992